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**From:** Fielding, John [mailto:[JFielding@thescottgroupdc.com](mailto:JFielding@thescottgroupdc.com)]  
**Sent:** Monday, June 05, 2006 2:26 PM  
**To:** ChangeInControl  
**Cc:** Kantor, Douglas  
**Subject:** Sound Banking Coalition Comments on Home Depot ILC Application

Attached are the comments of the Sound Banking Coalition in opposition to Home Depot's ILC application.

Please contact me if you have any questions or difficulties with the attachment.

Thank you.

John Fielding  
The Scott Group, PLLC  
3050 K Street, NW, Suite 400  
Washington, D.C. 20007  
tel: 202-342-8474  
fax: 202-342-8451  
[JFielding@thescottgroupdc.com](mailto:JFielding@thescottgroupdc.com)

June 5, 2006

Mr. John F. Carter  
Regional Director  
Federal Deposit Insurance Corporation  
25 Jessie Street at Ecker Square  
San Francisco, California 94105

**Re: Comments Regarding The Home Depot's Proposed Acquisition of EnerBank USA**

Dear Mr. Carter:

The undersigned members of the Sound Banking Coalition— the Independent Community Bankers of America, the National Association of Convenience Stores, the National Grocers Association, and the United Food and Commercial Workers International Union— submit this letter in opposition to The Home Depot's proposed acquisition of EnerBank USA, a Utah industrial bank<sup>1</sup> (the Bank). In connection with its proposed acquisition, The Home Depot (the Company) has submitted an Interagency Notice of Change in Control (the Notice) to the Federal Deposit Insurance Corporation (FDIC).

We urge you to reject the application. Given the pending Wal-Mart application, there is a clear and growing trend of commercial firms operating ILCs. It is inconceivable that the FDIC would approve these applications give the controversy of these applications, especially without clear Congressional authority to virtually obliterate the historic limits on ILCs.

As an initial matter, we note that a great deal of the information provided by the Company to the FDIC with the Notice is not publicly available. This includes the stock purchase agreement, the terms of which govern the Company's purchase of all the stock of the Bank; the Company's financial information; and the Company's business plan for the Bank. Public release of this information is needed to allow for full, meaningful comment on the proposed acquisition. We respectfully request that the FDIC: 1) make available to the general public all the withheld information, and 2) extend the comment period to provide the public 30 days to comment on the application following the release of this additional information. In addition, in light of the significant policy issues raised by this application, we request that the FDIC hold public hearings on the application to allow for a full airing of all the questions and issues surrounding Home Depot's proposed acquisition.

The Company's application raises significant policy issues. The mixing of banking and commerce that would occur if the Company owned the Bank, as well as the lack of consolidated

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<sup>1</sup> Industrial banks are alternatively referred to as Industrial Loan Companies or ILCs in these comments.

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supervision of the Bank by the Federal Reserve Board threaten some of the basic underpinnings of banking regulation in the United States. These threats are particularly acute here given the Company's plans for the Bank. Although we do not have access to the Company's complete business plan, the publicly available information provided in the Notice and the Company's press release announcing the proposed acquisition clearly contemplate a blurring of the lines between the Company's commercial activities and the Bank's lending activities.

The Company's Notice clearly states that the Bank and the Company "share a common focus on the home improvement market." Further, the document notes that the Bank's relationships with contractors and trade professionals "fits with The Home Depot's desire to expand its relationships with contractors and trade professionals – especially the local, small contractors that are core to The Home Depot's business." Although the Notice states that no Bank loan will be tied to purchases from the Company, it remains unclear to us exactly how this relationship will work without leading to consumer confusion regarding the status and identity of the lender. The scheme risks significant consumer confusion as to where the division between the Bank and the Company lies. Although the Notice does not provide details about the Company's statement that no EnerBank loan will be tied purchases at Home Depot stores, it seems reasonable to assume that borrowers might feel some pressure from contractors who do business with the Company to borrow from EnerBank. In addition, although the Company forswears explicitly tying loans with product purchases, there is no discussion in the Notice as to whether there will be other incentives for borrowers to become Home Depot customers or vice versa.

Although we have limited information regarding Home Depot's business plan, the Company appears to intend to use contractors – likely Home Depot customers – to market EnerBank loans to the clients for whom the contractors are working. This business model raises serious consumer protection concerns. As we have mentioned, the arrangement can easily confuse consumers, who may find it difficult to distinguish among Home Depot, the Bank, and the contractor. Who is providing the loan? For what may the loan proceeds be used? To whom is the loan to be re-paid? What is the relationship among Home Depot, the Bank, and the contractor?

In addition, the arrangement complicates compliance with Truth in Lending Act and related consumer protections governing disclosures, interest rates, predatory lending, and so forth. The contractors who, under the business plan, will serve as the initial contacts with the consumer will not be loan officers, indeed, they will not be employees of either the Company or the Bank. Who will ensure that consumers are protected to the full extent of the law? Whose responsibility is it to make sure consumers receive the right disclosures and other information legally required – and necessary to make an informed decision? While much of the legal responsibility may fall on the Bank, who will enforce it? In the absence of holding company oversight, will the Company be held responsible for violations?

The mixing of banking and commerce contemplated by the Company's business plan has serious ramifications for consumers that must be fully explored. Unfortunately, due to the lack of information made publicly available with this application, we are left with more questions than answers regarding how the Bank will operate and its relationship to Home Depot.

### **Home Depot's Acquisition of EnerBank Would Pose a Threat to FDIC Insurance and the Banking System**

In addition to these policy considerations, the Company fails to meet the criteria that the FDIC must consider in reviewing insurance applications under Section 6 of the Federal Deposit Insurance Act because the Company's ownership of the Bank would present a grave risk to FDIC insurance. The Company's proposed acquisition magnifies, and potentially exacerbates, the policy problems that arise out of the ILC loophole:

- The Company, as the holding company of an industrial bank, would not be subject to the same level of regulatory oversight as banks or bank holding companies: it would not face the same consolidated supervision at the holding company level, it would not be subject to consolidated capital requirements, and would be subject to arguably weaker regulatory enforcement, and
- the acquisition will entail the mixing of banking and commerce in a way that is not present with the Bank's current owner, CMS Energy Corporation.

This leaves insufficient safeguards to ensure that the Company and the Bank will not endanger the FDIC insurance.

We question the rationale for this differential treatment of ILCs. When you strip away the arguments about the regulation of ILCs by the FDIC and the states, you get a basic question that ILC supporters have never adequately answered – if holding company level regulation by the Federal Reserve is not necessary for ILCs, why is it necessary for other state and federally chartered banks? The arguments made by ILC supporters, if they were valid, would prove too much. They would demonstrate that the fundamental underpinnings of bank regulations for safety and soundness are unnecessary and an incredible waste of resources. Of course, in our view that is not the case. Indeed, consolidated supervision by the Federal Reserve is essential – and should apply to ILCs. The GAO recently reported to Congress that “from a regulatory standpoint, these ILCs may pose more risk of loss to the bank insurance fund than other insured depository institutions operating in a holding company.”

- **Consolidated Holding Company Supervision:** The Company, as the parent company of the Bank, would not be subject to consolidated holding company supervision. Although the Bank would be subject to FDIC oversight, the FDIC has more limited regulatory powers with respect to holding companies and affiliates than does the Federal Reserve. The Bank Holding Company Act

(BHCA) provides the Federal Reserve with the authority to examine the bank holding company itself and any of its non-bank subsidiaries at any time, while the FDIC has only limited examination authority, and is unable to examine affiliates of banks unless necessary to disclose the direct relationship between the bank and affiliate and the effect of the relationship on the bank.<sup>2</sup>

- **Consolidated Capital Requirements:** The Federal Reserve is also entitled to establish consolidated capital requirements to ensure that bank holding companies are a source of financial strength for the subsidiary bank. This source of strength doctrine has been codified in Regulation Y, which specifies that a bank holding company parent should be ready to provide capital to its bank subsidiary when needed. Failure to provide such assistance would enable the regulator to take enforcement action to protect the bank. In contrast, corporate parents of ILC's are not subject to these capital requirements.
- **Enforcement:** Finally, the Federal Reserve has broad enforcement authority under the BHCA, and can issue cease and desist orders, impose civil penalties, and order a holding company to divest non-bank subsidiaries if it determines that ownership of the subsidiary presents a risk to the financial safety, soundness, or stability of an affiliated bank and is inconsistent with sound banking principles or the purposes of the BHCA.<sup>3</sup> The Federal Reserve is the only federal agency authorized to take such actions against bank holding companies.

The safeguards provided by Federal Reserve regulation are necessary to protect the FDIC insurance fund against the potential risks presented by a bank owned by a major retailer such as the Company. Without these safeguards, it may be impossible for problems to be identified and managed in time to prevent deficiencies and damage to the federal safety net. This is particularly important with respect to the financial relationship between the Company and the Bank. The Notice clearly states that the Company will provide the Bank with the "capital required for EnerBank's growth" including up-front and on-going investments of equity to enable the Bank to meet required leverage and risk ratios, as well as a line of credit.

Although the Bank may welcome the Company's financial support, this could change if the Company finds itself in financial difficulties. One of the factors the FDIC is required to consider in determining whether or not to grant federal deposit insurance is "the adequacy of the depository institution's capital structure." Unfortunately, we are unable to comment on the Company's current capital structure due to the inadequacy of the public information available in connection with the Notice. We urge the FDIC to be more forthcoming with such information.

There is a temptation to assume that because the Company is large and has many assets, it is safe. We have seen this assumption proven wrong time and time again. In fact, if anything,

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<sup>2</sup> Letter to Senator Tim Johnson from Alan Greenspan, Chairman of the Board of Governors of the Federal Reserve System, June 25, 2003, at 4.

<sup>3</sup> *Id.* at 5.

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U.S. economic history has often shown that a far different adage typically holds sway – the bigger they are, the harder they fall. Enron, Worldcom, and Kmart provide recent examples. In fact, the latest example is playing out before our eyes as we watch General Motors lose billions of dollars each year and dramatically cut its workforce to try to stay solvent. Fifty years ago no one would have believed that GM would be in the difficult situation it is in today. What will this mean for GM's ILCs? Without regulation by the Federal Reserve that is very hard to say. Perhaps the ILCs are sound and will remain so for years to come – but perhaps not. The problem is that no one really knows because even though GM owns more than one bank it is not subject to consolidated supervision. We are left to wait and see what the future holds. These examples do make one thing clear – size and large revenues do not guarantee safety.

The Federal Reserve on numerous occasions has opined on the threat posed by ILCs to the banking system and the insurance fund. In a letter to Representative James Leach (R-IA) on January 6, 2006, for example, then Federal Reserve Board Chairman Alan Greenspan described the current and growing threat to the nation's financial system posed by ILCs.

When this exemption was adopted in 1987, ILCs were mostly small locally owned institutions that had only limited deposit-taking and lending powers. However, much has changed since 1987 and recent events and trends highlight the potential for this exemption to undermine important general policies established by Congress that govern the banking system and to create an unlevel competitive playing field among banking organizations. The total assets held by ILCs have grown by more than 3,500 percent between 1987 and 2004, and the aggregate amount of estimated insured deposits held by ILCs has increased by more than 500 percent since 1999.

The character, powers and ownership of ILCs have changed materially since Congress first enacted the ILC exemption. These changes are undermining the prudential framework that Congress has carefully crafted and developed for the corporate owners of other full-service banks. Importantly, these changes also threaten to remove Congress' ability to determine the direction of our nation's financial system with regard to the mixing of banking and commerce and the appropriate framework of prudential supervision. These are crucial decisions that should not be made through the expansion and exploitation of a loophole that is available to only one type of institution chartered in a handful of states.

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Then, in February of this year, newly-appointed Federal Reserve Board Chairman Ben Bernanke testified before the House Financial Services Committee and urged Congressional review and action with respect to the regulation of ILCs.

Like the Federal Reserve, a number of public interest groups including the Consumer Federation of America, National Consumer Law Center, ACORN, Consumers Union, National Association of Consumer Advocates, National Community Reinvestment Coalition, and the U.S. Public Interest Research Group have raised concerns about the public policy implications of the industrial bank loophole in the BHCA.<sup>4</sup>

The depth and breadth of the concern about the ILC loophole has radiated across the country. In the absence of federal leadership, states are taking matters into their own hands. Nearly a dozen states have adopted or are considering legislation that would block or limit ILC holding companies from using ILC charters to open bank branches within their borders. In Iowa, Virginia and Maryland, new laws ban ILC branches on the premises of a commercial affiliate. Laws in Missouri, Vermont and Wisconsin would prohibit ILCs from doing any business in their states. Similar legislation is pending in Illinois. Michigan and Pennsylvania would specifically bar branches of ILCs chartered in Utah. Kentucky and New York are considering similar legislation. This state activity is indicative of nationwide concerns about this issue.

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The Company's proposed acquisition of the Bank is troubling on many fronts and should be rejected. Because it clearly poses a threat to FDIC insurance, the proposal does not meet the basic legal requirements upon which the FDIC judges such applications, and it would broaden the ILC loophole in the BHCA and endanger U.S. policy which has kept banking and commerce separate and strong for decades. We urge you to deny the Company's request.

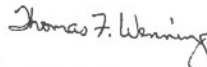
Sincerely,



Vice President, Congressional Relations  
Independent Community  
Bankers of America



Senior Vice President  
Government Relations  
National Association of Convenience Store



Senior Vice President  
and General Counsel  
National Grocers Association



Legislative and Political Affairs Director  
United Food and Commercial  
Workers International Union

<sup>4</sup> See Testimony of Travis Plunkett, Legislative Director, Consumer Federation of America and Carolyn Carter, Of Counsel, National Consumer Law Center, before the Senate Committee on Banking, Housing and Urban Affairs, hearing titled "Current Proposals Considered for Regulatory Relief Legislation," June 21, 2005.